

**Testimony of**  
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**and**  
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**On the Issue of**  
**Simplification of Sales and Use Tax Law**  
**and Taxation of Remote Commerce**

**Before the**  
**United States Senate**  
**Committee on Commerce, Science, and Transportation**

**The Honorable John McCain, Chairman**

**March 14, 2001**

Mr. Chairman and Members of the Committee, I am Elizabeth Harchenko, Director of the Oregon Department of Revenue and Chair of the Multistate Tax Commission. It is an honor to appear before this committee. The Multistate Tax Commission is an interstate compact agency with 45 participating states, including the District of Columbia. The Commission works to preserve federalism and to promote fairness, uniformity, and simplification in state and local tax systems.

Thank you for this opportunity to address the most important issue of federalism facing our nation today. That issue is whether Congress will join in partnership with the states to support their efforts to ensure that all commerce, from local to global, is treated in an equal, uniform, and non-discriminatory manner by state and local tax systems. A federal/state partnership is essential to support the free flow of commerce and fair competition in the national marketplace. Forging this partnership will influence the speed and extent to which the benefits of modern technology and economic prosperity spread from one state and region to another. Finally, developing this partnership will shape the future of federalism. It will determine whether states and local governments will be able to perform the role and functions that the nation, including Congress, expects them to perform in supporting the national economy, ensuring the quality of life for all citizens, and doing so efficiently and effectively. Why is it so critically important that Congress join the states in such a partnership? Because the principles on which our nation was founded recognized that the states would work cooperatively through our national government, and that the national government has the power and the resources to support and participate in these joint efforts.

All states and local governments tax their own residents and nonresidents who engage in local and interstate business through different mixes of income, business activity, sales and use, excise and other taxes depending upon local circumstances. Regardless of the types of taxes states and local governments choose to levy, those taxes must apply equitably to all forms of commerce. In this regard, we should all understand that it was never the constitutional intent of the Commerce Clause to deprive states of the ability to ask for a "fair share" contribution from interstate business to support governmental services. Tax policy should not play favorites: similar economic activities should be taxed in similar ways to support the free flow of commerce and equal competition. So balance and equity in taxation between local and interstate commerce is economically essential and constitutionally appropriate.

The greatest imbalance in state and local taxation arises in the area of the collection of sales and use taxes. There is no sound tax policy that supports a tax being collected on a shirt or a music recording or a computer sold through a local store, but not collected when the same product is sold by mail order or through the Internet. States recognize that we must do our part to correct this imbalance by simplifying state and local taxes so that the collection of these taxes does not create an undue burden on interstate commerce. Through the Streamlined Sales Tax Project, the states—working side-by-side with business—have developed measures that will radically simplify sales and use taxes and eliminate undue burdens that may be associated with their collection. In light of this development, Congress should join in partnership with the states and act to level the playing field between local and remote commerce by requiring remote

sellers, with sales greater than a national threshold amount, to collect sales and use taxes for those states implementing the Streamlined Sales Tax Project recommendations. Doing so will achieve fundamental fairness and non-discrimination in the application of sales and use taxes between local business and interstate commerce.

Within the context of this partnership, Congress also needs to examine technical language in the Internet Tax Freedom Act —should Congress choose to extend that act for any period— that may exacerbate existing inequities in sales and use taxation. In particular, Congress needs to address the potential for some sellers to bundle extensive services with Internet access and thus avoid sales and use taxes, when other sellers will still be required to collect taxes on those services. Congress should address as well ambiguous provisions in the current definition of discriminatory taxes that may, unwittingly, be encouraging new discrimination in the collection of sales and use taxes.

In addition to encouraging a federal/state partnership, we ask Congress to refrain from making any of the current inequities worse. In particular, Congress should not enact new restrictions on the ability of states to tax a fair share of the income of multistate enterprises. The proposals advanced by some business interests would dramatically change current law and would simply create and multiply within the business activity tax realm the same problems that have existed for sales and use taxes. These proposals would allow a select group of companies to avoid their fair share of state and local taxes and to shift that burden to wage-earners, small

businesses and traditional manufacturing and natural resource industries—all of which are captive within the taxing state.

Congress should recognize that in an era when companies can make substantial quantities of sales and earn substantial income within a state from outside that state, the concept of “physical activity” as a standard for state taxing authority is inappropriate. Among other problems, this concept discourages the free flow of investment across state boundaries and restricts the spread of economic prosperity from areas of initial investment to all states and regions. If a company is subject to state and local taxes only when it creates jobs and facilities in a state, then many companies will choose not to create additional jobs and invest in additional facilities in other states. Instead, many companies will choose to make sales into and earn income from the states without investing in them. If Congress ties states to physical activity concepts of taxing jurisdiction, Congress will be choosing to freeze investment in some areas and prevent the flow of new technology and economic prosperity in a balanced way across the nation. Congress should recognize that a standard of physical activity for tax nexus is not in the best interest of our nation, and that sound economic policy requires adoption of practical concepts of economic nexus as a standard for the application of state and local taxes.

Finally, let me briefly address how the nation as a whole, its corporate citizens, and its taxpayers benefit from strong state and local governments and a strong federal/state partnership. The nation relies on states and local governments to educate their citizens for a modern economy and society. It relies on states and local governments for civil order and a

framework of commercial law that supports orderly commerce. The nation relies on states and local governments to provide the infrastructure over which commerce flows. It relies on states and local governments to adopt policies that ensure the flow of electrical energy across state boundaries so that the new, technology-based economy can flourish. The genius of our system of federalism is that our nation relies on states and local governments to tailor vital services of national benefit to fit local circumstances. If this system of federalism is to continue to serve this nation well in this new century, then Congress and states must form a partnership to ensure that interstate commerce participates on a full and equal basis to help finance the state and local services that benefit the entire nation.

Mr. Chairman, thank you for the opportunity to address the committee. I will be happy to answer any questions that you or the Committee members may wish to pose.